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UNCLAS SECTION 01 OF 02 YEREVAN 000966

SIPDIS

SENSITIVE

E.O. 12958: N/A

TAGS: [ECON](#) [ENRG](#) [EPET](#) [AM](#)

SUBJECT: IRAN-ARMENIA PIPELINE: WHAT IF THEY HAVE THE MONEY?

Ref: A) YEREVAN 382 B) YEREVAN 698 C) YEREVAN 816

1. This cable is sensitive but unclassified. Please protect accordingly.

SUMMARY

2. (SBU) Post has consistently discredited recent media reports about the ten-year-old proposal to build a pipeline from Iran to Armenia on the grounds that there has been no indication of a source for the USD 120 million to build the Armenian portion of the pipeline. Although we still believe that the Armenian government has no money for the project, recent comments made by the Foreign Minister, the Iran desk officer and the Ministry of Energy suggest that officials in the government are themselves convinced that they will find funding. Suggestions of an electricity for gas swap persist despite denials by the Ministry of Energy. So for argument's sake we will assume that the government is able and willing to spend USD 120 million to build its portion of the pipeline--What then? End Summary.

STILL LOOKING FOR MONEY...

3. (SBU) On April 22, 2004, a resident Amcit who represents a U.S.-based foundation, called on the Ambassador to discuss the potential pipeline deal. According to the American, the Foreign Minister asked him for technical and financial advice in connection with GOAM efforts to raise the money to pay for a pipeline bringing Turkmen gas through Iran to Armenia. He noted that the Government of Armenia was searching for help and advice on how to finance the proposed pipeline. (Note: The Amcit was concerned about U.S. policy and law and indicated after our conversation he would not be engaging in this area. End Note.)

...BUT OPTIMISTIC

4. (SBU) High-level Armenian officials are more and more confident that they will somehow find the money to pay for the Iran-Armenia pipeline. In a recent interview, President Kocharian acknowledged a preliminary deal with Iran on the pipeline. Just back from a state visit to Iran, the Foreign Minister, Vartan Oskanian, told the Ambassador that the Iranian Minister of Oil would visit Yerevan May to sign a final deal. Asked about the money to build the pipeline, "I think the money will appear somewhere," he said. Similarly, Garnik Badalian, Iran Desk Officer at the MFA, told us that after the Iranian Minister's visit, the government was planning to launch a feasibility study on the pipeline. According to Badalian, the discussion so far has included "no specific financial negotiations" and it has just been assumed that each side will build its own part.

ELECTRICITY FOR GAS SWAP?

5. (SBU) Reports that Iran and Armenia intend to sign a deal to swap electricity for gas are persistent. Both the Foreign Minister and the MFA's Iran desk officer raised the idea, saying that both sides agree in principle to such an arrangement. "Bull****," said Deputy Minister of Energy Areg Galstyan when we called to confirm the report. (Note: Galstyan insists that he is one of three people privy to the details of the negotiations. End Note.) Badalian added that there would be a lot of problems to be worked out in any swap deal. Not least must be the fact that the Government of Armenia doesn't own the electricity and the Government of Iran doesn't own the gas. The GOAM has privatized the lion's share of Armenia's electricity generation resources, and RAO UES, a Russian energy company, controls 80 percent of it. Those assets remaining in the government's control, notably the Vorotan Cascade hydro plant, generate too little electricity (between 700 and 1300 GWh per year, depending on water levels) to exchange for substantial amounts of gas. If Iran were to purchase gas from Turkmenistan to exchange with Armenia at a set rate for

electricity, it would expose itself to risk based on the fluctuations in the gas market. Ultimately, any swap would have to involve private actors on both ends.

WHAT IF RAO IS INVOLVED?

16. (SBU) Assuming RAO UES and the gas supplier could be involved, would the swap be reasonable? Iran and Armenia have been swapping electricity for years, with Armenia sending excess electricity to Iran during Iran's peak usage in summer in exchange for electricity in winter, Armenia's peak usage time. Armenia's excess generating capacity during summer, Iran's peak usage time, is roughly 200 MW, enough for considerable electricity transfers abroad. It is gas-fired energy (which is more expensive than nuclear or hydro-electricity) that composes any margin of extra electricity that Armenia produces, thus any export of electricity necessarily involves burning gas to generate that extra electricity. In order for this to justify the expense of building the pipeline, Armenia would have to receive significantly more gas than is necessary to produce the electricity it exchanges, an unlikely long-term deal.

IRAN COULD BE CHEAPER WAY TO GET TURKMEN GAS

17. (SBU) Nonetheless, once built the pipeline could be a cheaper way to get gas from Turkmenistan. The gas that Armenia currently receives through the pipeline from Russia through Georgia is also from Turkmenistan. Its price at the Armenian border is USD 55.00 per thousand cubic meters; the wellhead price is USD 42.50. Assuming that the transit this way could capture USD 10 per thousand cubic meters, gas could arrive more cheaply than from the current pipeline. At the full capacity of 1.5 billion cubic meters per year, there could be USD 15 million per year in transit revenue--arguably enough to justify the USD 100 million to build the Iranian side of the pipeline.

COMMENT

18. (SBU) While it is clear that the Armenians want the pipeline, it is equally clear that many of the important details, such as paying for the pipeline and for the gas after that, have yet to be worked out. In one step towards reality the President has scotched all talk of the pipeline continuing through Armenia to serve Georgia and Europe. While reports of a swap of gas for electricity appear to be not entirely credible, it is possible that the governments will add, as part of the contract, terms of trade for swaps of small amounts to cover Iran's energy shortages in the summer. Whether or not Armenia manages to find the money to begin construction on a pipeline this year, its long-term strategy must include some diversified energy sources. Looking forward to the inevitable, if deferred, closure of the Armenia Nuclear Power Plant, the GOAM remains unwilling to depend on the single gas pipeline through Georgia for 80 percent of its energy needs.
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